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DIVIDEND POLICY AND WEALTH CREATION BY FIRMS QUOTED ON THE NIGERIA STOCK MARKET: A STUDY OF NSE-30 INDEX

Iriobe Grace O.
Department of Financial Studies, College of Management Sciences,
The Redeemer's University, Ede, Osun State, Nigeria.
e-mails: iriobeog@gmail.com; benignbekkie@yahoo.com

Abstract
Dividend policy has remained one of the most important issues in Corporate Finance. This study examined the relationship between the proxy of dividend policy, dividend payout ratio and the proxies of firms' wealth creation like capital structure, profits and investment. Panel Least Squares (PLS) regression model was used to investigate the effect of dividend policy on wealth creation by firms in Nigeria. Data were extracted from the financial statements of 30 firms listed on the Nigerian Stock Exchange Index (NSE-30 Index) and the NSE Fact Books for the period 2004 to 2010. The results showed that, in isolation, while capital structure had significant negative effect on dividend payout (t-stat p-value = 0.0089 < 0.05), profitability had significant positive effect (t-stat p-value = 0.0000 < 0.05); but fixed asset-dominated investment had insignificant negative effect as evidenced by t-stat p-value = 0.5969 > 0.05level of significance. On the aggregate, the wealth creation indices jointly significantly determined dividend policy of the firms as evidenced by the p-value of the F-statistic (p-value = 0.0000 < 0.05). This indicated that though wealth creation significantly determined dividend policy of the firms, payouts were explained more by factors other than these components of firms' wealth creation in Nigeria.

Keywords: Dividend payout ratio, capital structure, profitability, Investment, NSE-30 Index.

INTRODUCTION

Dividend policy remains one of the most important topics in Corporate Finance. Black (1976) in Almakawi, Rafferty & Pillai (2010) stated that significant attention has been given to thIs concept in order to solve the dividend puzzle "the harder we look at the dividends picture, the more it seems like a puzzle, with pieces that just do not fit together". Some researchers have dedicated their work to explaining the various factors and theories that determine a firm's decision to pay dividends or otherwise (Bhattacharyya 1979; Bhattacharyya, Amin and Morill, 2008). However, having considered and reviewed literatures on dividend policy, specifically as it relates to the creation of value and wealth, some gaps have been identified to include that available studies in Nigeria have only dealt with specific sectors in the financial market (Asogwa 2009; Amadasu 2011). This study intended to fill this gap by examining the dividends policy and shareholders wealth across sectors and industries on the Nigeria stock market, thereby contributing to knowledge and literature with specific reference to Nigeria.

The major justification for this study is that there are still unanswered questions about the

relationship that exist between wealth creation by, and dividend policy of, firms, and the effects of wealth creation drive by firms on their dividend policies. The considerable research efforts that have been devoted to examining the effects of dividend policy on wealth creation (Lie, 2005; Zhou and Ruland, 2006) suggest that available studies consider causation to run from dividend policy to wealth creation. However, this t study envisaged the possibility of dividend policy responding to wealth creation drive by firms in Nigeria for a period of seven years (2004-2010). The period in consideration is related to the different operating periods in the stock market. These are the 2004-2005 consolidation eras for all financial institutions on the NSE, 2006-2007 the post consolidation period for all institutions on the NSE, and lastly, 2008-2010 the stock market crash due to global meltdown. However, this study is delimited to the NSE-30 index. These 30 companies will be considered because of their market capitalization and liquidity in the Nigeria stock market.

LITERATURE REVIEW

Dividend Policy in Nigeria

Nigerian firms and industries have grown tremendously over the years and one of the attributes of these successes is the dividend policy seen to be in the Nigerian business environment. Akinsulire (2011), states that dividend policy is extremely important because of its announcement effect on share values. He further explains that a stable dividend policy is expected to lead to higher share prices because of the greater confidence of investors about future prospects of the firm. For a company in Nigeria, it is a pivotal policy around which other financial policies rotate (Alii et al., 1993 in Uwuigbe, Jafaru and Ajayi, 2012). However, Ullah, Fida and Khan (2012) posit that dividend policy is an influential control vehicle to reduce the conflicting interests of the shareholders and managers because shareholders are interested in getting dividends, but managers prefer to retain earnings. In their views, managers want to retain earnings for maintaining higher control over the resources. Adefila, Oladipo and Adeoti (2013) have the opinion that the optimal dividend policy of a firm depends on investors' desire for capital gains as opposed to income, their willingness to forgo dividend now for future returns, and their perceptions of the risk associated with postponement of returns. Ramesh & Nimalathasan (2011) considered dividend policy as one of the most crucial issues for management decision, because it serves as a communication tool between management and investors and, to them, investors do not always trust managers to provide unbiased information about their companies' prospects, but

dividend signals are relatively reliable, because they require cash payments and cash cannot be easily manipulated. In line with this, Nissim & Ziv, (2001) in Ajanthan (2013), states that dividend policy is seen as the regulations and guidelines that a company uses to decide to make dividend payments to shareholders. Hence, the dividend decisions of firms are the primary elements of corporate policy. Ogbulu & Arewa (2011), defined dividend policy as what proportion of earning to a firm need pay out as dividends. Dividend policy, in the context of this study, means the payout policy that managers follow in deciding the size and pattern of cash (or non-cash) distribution to its shareholders or investors over a certain period of time.

Theoretical and Empirical Literature

A vast number of researchers examined those factors that are the major determinants of dividend policy. One aspect of this literature investigated the theories that explained the relationships between dividend policy and wealth/value creation by firms. The first theory that explains the relationship between dividend payouts and profitability is the Bird-In-Hand Theory, which is of the opinion that high dividends actually increase value of shares and in turn, firms' values. Based on this opinion, investors prefer the "bird in the hand" of cash dividends rather than the "two in the bush" of future capital gains (Almakawi et al., 2010). Therefore, increasing the dividend payments to shareholders, ceteris paribus, can be associated with increases in firm value. As paying a high current dividend may reduce the uncertainty about future cash flows, a high dividend payout ratio will reduce the cost of capital, and in turn increase the value of shares. That is, according to the "bird-in-the hand" theory, high dividend payout ratios maximize a firm's value. However, Graham and Dodd, for instance, argued that a dollar of dividends has, on average, four times the impact on stock prices as a dollar of retained earnings (Almakawi et al., 2010). However, the link between shareholders wealth and dividend policy was earlier explained in the work Gordon (1959) that there are three possible reasons why investors would want to buy a certain stock. First is to obtain both dividends and earnings, second is to obtain dividends, and finally, to get the earnings. He discovered that dividends have a great influence on share price than retained earnings. Also, he argued that the required rate of return on a share increases with the fraction of retained earnings because of the uncertainty associated with future earnings. Also, the Pecking Order Theory of Myers (1984) described the relationship of dividends policy, capital structure and investments in determining the actual payouts of firms. This theory described the relationship as when firms prefer to finance their operations with internally generated funds to avoid the under investment problem associated with risky debt and informational

asymmetries between managers and the security markets. If firms do not have sufficient internally generated funds to finance their operations they will issue debt to finance their financial deficit. Only in extreme cases will they finance their financial deficits with external equity capital. Firms shifting to the pecking order theory in financing their operations will seek to avoid raising external capital by maximizing the amount of internally generated funds available to finance their operations. One obvious way to accomplish this is by reducing the amount of dividends paid to the firm's shareholders. Therefore, if a large number of firms shifted to the pecking order theory in financing their operations this could account for the reduction in the propensity of firms to pay dividends. Fama and French (2002) empirically tested the implication of the pecking order theory and recommend that if firms' are cutting their dividend payments in accordance with the theory then firms should also be reducing the amount of debt financing they use to finance their operations as well. Julio and Ikenberry (2004) observed that firms are now shifting away from the pecking order theory in financing their operations. That is, these firms would no longer feel the need to maximize the amount of their internally generated funds by minimizing dividend payments and might start to increase the dividends paid to shareholders.

Adefila, Oladipo & Adeoti (2013), made efforts to discuss the issue of how much a company should pay its stockholders, since dividend is one that has been of concern to managers for a long time. According to these researchers, the optimal dividend policy of a firm may be defined as the best dividend payout ratio the firm can adopt. Their study examined the relationship between dividend policy and the value of a firm and in so doing; they adopted the methodology of Person's Product Movement Correlation to evaluate the data collected from the fifteen studied companies, but the current studied used the multiple regression analysis to explain the relationship between the variables. Also, Badu (2013) examined the determinants of dividends payout policy of listed financial institution in Ghana using fixed and random effects. He employed Panel data for a period of 5 years from selected companies. In his result, he showed that there is a statistical significant and positive relationship between Age and liquidity but saw statistically insignificant relationship between profitability, collateral and dividend payment, but Rafique (2012), made effort to reveal the insight dynamics for the determination of dividend payout with reference to non financial firms listed in the Karachi Stock Exchange. He then identified key explanatory variables to the determination of dividend payout as Earnings, Firm Size, Growth, Profitability, Corporate Tax and Financial Leverage. Hence, Regression was run in isolation using OLS of the Multivariate Regression Analysis, once with earnings and once with profitability along with

testing the two together in a third regression test. Regression Results of all three regressions were consistent. His results revealed that Corporate Tax and Firm's Size had significant relationship with Dividend Payout. Rests of the four explanatory variables were found to be insignificant in context of Pakistani markets. The current study is similar to that of Rafique (2012) but for the financial firms in Nigeria, and variables used for analysis.

Furthermore,, Gul et al, (2012), examined the influence of dividend policy on shareholder's wealth of 75 companies listed in "Karachi Stock Exchange", for a period of six years from 2005 to 2010 using multiple regression and stepwise regression. Shareholder's wealth serves as a dependent variable which is measured as dividend per share, whereas the explanatory variable, dividend policy, is measured as profitability, liquidity, leverage, growth and company size in their study. They made use of data from company's annual reports, Karachi Stock Market and State Bank of Pakistan. There result and findings shows significant influence of dividend policy on wealth of shareholder's, as far as the dividend paying companies are concerned. In line with this, the current study will examine the influence of wealth creation by firms on their dividend policies.

DATA, METHODOLOGY AND MODEL

Data Sample and Characteristics

The data and variables used in this study relates to the Nigerian stock market and based on the Perking Order theory with the opinion that firms prefer to finance their operations with internally generated funds to avoid the under investment problem associated with risky debt and informational asymmetries between managers and the security markets and the Bird-In-Hand Theory of high dividends actually increasing the value of shares and in turn firms' values. Hence, the opinion that firms would no longer feel the need to maximize the amount of their internally generated funds by minimizing dividend payments and might start to increase the dividends paid to shareholders Julio and Ikenberry (2004); therefore, an obvious relationship between wealth creation and dividends payment. To verify this relationship in this study, variables used are dividends payout ratio (DPR) as proxy for dividend policy; capital structure (CS), Profitability (PR) and investment (INV) as proxies for wealth creation by firms in Nigeria. The data for these variables as they are used for panel least square analysis in this study is presented in Appendix I.

This study attempted to generate the relationship between dividend payout ratio and other wealth creation variables (explanatory variables). The study therefore employed a panel data analysis by running a regression to verify in quantitative terms how the explanatory variables

impact on the value of the dependent variable. The data obtained were fitted to the linear equation by Panel Least Square (PLS) technique of model estimation.

The Model

This study used a multiple linear regression equation model. Theoretically, the model was specified on the assumption that wealth creation by a quoted firm is the determinant of dividend policy of the firms. Using the Dividend Payout Ratio (DPR) as a proxy or surrogate for dividend policy, since it is the pivot around which dividend policy revolves and assumed to be determined by wealth creation drive of firms. The model expressed DPR as a function of wealth creation by quoted firms. Functionally therefore,

$$DPR = f(CS, PR, INV)$$

where,

DPR= Dividend Payout Ratio

CS= Capital Structure

PR= profitability

INV= Investments

The model is expressed in its stochastic form as follows:

$$DPR = \beta_0 + \beta_1 CS + \beta_2 PR + \beta_3 INV + \mu$$

Where β_0 is the intercept of the model. It is the level of dividend payout ratio the firms can sustain when wealth creation is considered irrelevant. β_i (i = 1, 2, 3) are the coefficients (effects) of the respective components of wealth creation by firms and each measures the effect of associated wealth creation component on dividend policy. μ is the stochastic variable introduced into the model to accommodate the influences of other variables that may shape dividend policy of the firms but which are not explicitly included in the model.

Technique for Model Evaluation

Numerical values of the intercept and coefficients (effects) of wealth creation variables on dividend policy were evaluated in two stages. First was to show the nature of relationship between proxy variable of dividend policy and proxy variables of wealth creation by firms in relation to the a priori expectation. Second was to determine the significance or otherwise of partial/isolated and aggregate effects of wealth creation dimensions on dividend policy.

The significance of isolated effects or otherwise of wealth creation components on dividend payout ratio were evaluated using the t-statistic. The significance of aggregate effects or

otherwise of wealth creation components on dividend policy variable were evaluated using the F-statistic.

A Priori Expectation

The firms are expected to sustain some level of dividend policy even in the absence of the wealth creation components, and CS was expected to exert negative effect on dividend policy; PR was expected to exert positive effect on dividend policy; and INV was expected to exert negative effect on dividend policy.

Table 1: Summary of A Priori Expectation

Variables	Acronyms	Expected effect
Capital Structure and Dividend Policy	CS_{DP}	Negative
Profitability and Dividend Policy	PR_{DP}	Positive
Investments and Dividend Policy	INV_{DP}	Negative

Source: Researcher's model, 2015

DATA ANALYSIS AND PRESENTATION

Table 2: Regression Analysis Result and Estimated Model

Variable	Coefficient	Std. Error	t-statistic	Probability	Significance
Intercept β_0	0.284118	0.123392	2.302565	0.0223	
Capital Structure	− 0.453777	0.171843	− 2.640653	0.0089	Yes
Profitability	0.713709	0.125097	5.705239	0.0000	Yes
Investment	− 0.036270	0.068470	− 0.529729	0.5969	No
R-squared	0.158383		F-statistic	12.92230	
Adjusted R- squared	0.146126		Prob(F-stat)	0.000000	

Source: Eviews7 Regression Output (See Appendix II)

Estimated Model:

DPR = 0.28 – 0.45CS + 0.71PR – 0.04INV

t-stat = 2.30 – 2.64 + 5.71 – 0.53

A Priori Expectation:

The estimates of the coefficients of the model indicated that the effect of CS, PR, and INV respectively on DPR are consistent with the pre-estimation expectations as indicated by the respective signs ($\beta_1 = -0.453777 < 0$; $\beta_2 = 0.713709 > 0$; $\beta_3 = -0.036270 < 0$) Thus, the result shows that when CS and INV are on the increase, there will be a fall in DPR. When PR

increases, there will also be an increase in DPR.

The Regression Result

Isolated Effect of the Regression Result:

The table 2 above showed that the probability associated with the t-statistic of coefficient capital structure is less than the specified 0.05 level of significance (p-value = 0.0089 < 0.05). This provided empirical evidence that capital structure exerted significant negative effect on dividend payout of the firms during the study period. This implied that an increase in CS (financial leverage) caused a decline in equity capital and a fall in dividends payment. Therefore, with respect to capital structure (CS), research hypothesis H_o1 is rejected. Also, the probability associated with the t-statistics of coefficient profitability (PR) is less than the specified 0.05 level of significance (p-value = 0.0000 < 0.05). This indicated that the isolated effect of PR is positive and significant. This implied that an increase in profitability (PR) will lead to more dividends payment. Finally, the probability associated with the t-statistics of coefficient investment (INV) is greater than the specified 0.05 level of significance (p-value= 0.5969 > 0.05). This indicated that the isolated effect of INV is negative and insignificant. This means that growth in fixed assets will lead to less/no dividends payment. It implies that when firms tie down financial resources on fixed assets, it will reduce the available financial resources within the firm which will result in less or no dividends payment to shareholders.

Aggregate Effect of the Regression Result:

The probability associated with the respective F-statistics is less than the specified 0.05 level of significance. That is, probability (F-statistic = 0.0000 < 0.05). These implied that the components of wealth creation in this study jointly have a significant effect on dividend policy. Since the wealth creation components have significant overall effect on dividend policy, it can be concluded that, on the basis of this analysis, wealth creation has significant effect on dividend policy. With this decision, the general research question of this study is answered and the main objective of the study is achieved. Also, the components of wealth creation exhibited weak strength in explaining variations in dividend policy and payouts by the firms during the study period. This is shown by the coefficient of determination (R-Squared = 0.158383) that translated to about 15.8% of the variations in dividend payout being explained by the wealth creation variables while 84.2% variations were unexplained.

FINDINGS

For the period of 2004-2010, the following relationships were observed between dividend policy and wealth creation by firms in Nigeria which are significant for policy formulation. Capital structure had a negative significant relationship with dividend policy adopted by quoted firms in Nigeria. This means that as firms increase their borrowings there will be less dividend payments. Profitability had significant positive effect on dividend payout during the period and, as such, dividend payout increased and decreased reasonably with profit. Investment (in fixed assets) exerted negative effect on dividend payment. That is, the more the financial resources of the firms were invested in fixed assets, the less the dividend payout, and vice versa. This shows that the sampled firms in Nigeria consider investment as an insignificant factor in their various dividend policies. On the aggregate, those determinants of firms' wealth creation were found to exert significant effect on dividend policy of quoted firms. Thus, the components of firms' wealth creation are relevant in determining dividend policy. Also, the F-statistic has been found to be significant, implying that the model is fitted even with the low R^2 value. The weak strength of the wealth creation components suggested that, though the components were relevant to dividend policy, dynamics of dividend payout of the firms were driven more by some other factors of firms' wealth creation.

RECOMMENDATIONS

- Since profitability and capital structure drive dividends, firm managers may use dividend payments to inform the public on the competitiveness of their firms.
- The knowledge of dividend policy and its implementation should be improved upon by financial experts, accountants, finance managers and other related disciplines. This can be achieved by making dividend policy a major topic in the academic curriculum of the Nigerian Universities; institutes such as Chartered Institute of Bankers of Nigeria (CIBN), Institute of Chartered Accountants of Nigeria (ICAN); and other institutions of higher learning.
- Nigeria firms could establish and manipulate dividend policy to some extent in order to meet the expectations of the various stakeholders. This study could be of help in doing this since the result indicate that profitability is an important explanatory factor in the variability of dividend policy. Profitability largely depend on the working capital and other variables that are within (internal) the control of the firms.
- The Nigeria Stock Exchange and the Securities and Exchange Commission need to review the composition of the Nigeria stock market in order to completely eliminate

or minimize the porousness of the stock market. In the course of data analysis, it was observed that the removal/inclusion of some specific stock in the model will cause a significant/huge change in the result of the analysis. Therefore, there is need for the Nigeria government to put some policies in place, especially, to ensure the listing of some upstream and multinational companies who transact businesses in Nigeria but are not listed on the Nigeria Stock Exchange. The DG of Sec on 28th April, 2014 mentioned that efforts are made to encourage a relationship between the Nigeria stock market and the South Africa stock market such that South Africa firms operating in Nigeria (e.g. MTN and other telecommunication companies) can get listed on the NSE market.

CONCLUSION

This study has established that capital structure and profitability plays a very important role in determining the dividend payout policy of firms in Nigeria. The study has established the relevance in terms of specific and aggregate considerations. That is, their contribution to dividend policy was positive and the contributions were significant on the aggregate. Also, the contributions of the variables showed low strength in explaining dividend policy.

Results of the analysis and findings thereof have provided some interesting insights that will enhance clearer understanding of dividend policy and wealth creation by firms in Nigeria. Therefore, the findings are expected to stimulate more research interests to deepen the knowledge and understanding of dividend policy determination in all economies. When determining the firms' ability in establishing dividend policies using the variables identified by this study, depends on whether the firm is a high-growth/mature firm. This study concludes that the formulation of appropriate dividend payout policy is influenced by the firms' specific (internal) factors and some components of wealth creation by firms in Nigeria, and that the strengthening and enforcing of laws on dividend payment in Nigeria is necessary to ensure a more frequent payment by firms so as to increase their market values.

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Appendix I
Regression Analysis Results.

Dependent Variable: DPR
Method: Panel Least Squares

Sample: 2004 2010
Periods included: 7
Cross-sections included: 30
Total panel (balanced) observations: 210

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CAPITALSTRUCTURE	-0.453777	0.171843	-2.640653	0.0089
PROFITABILITY	0.713709	0.125097	5.705239	0.0000
INVESTMENT	-0.036270	0.068470	-0.529729	0.5969
C	0.284118	0.123392	2.302565	0.0223

R-squared	0.158383	Mean dependent var	0.431857
Adjusted R-squared	0.146126	S.D. dependent var	0.878642
S.E. of regression	0.811912	Akaike info criterion	2.440014
Sum squared resid	135.7954	Schwarz criterion	2.503769
Log likelihood	-252.2015	Hannan-Quinn criter.	2.465788
F-statistic	12.92230	Durbin-Watson stat	1.021504
Prob(F-statistic)	0.000000		

Source: EViews7- Enhanced Regression Output